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Report of the Board of Auditors on the capital master plan for the biennium ended 31 December 2003

Note by the Secretary-General

The Secretary-General has the honour to transmit the present report to the members of the General Assembly, pursuant to Assembly resolution 57/292 of 20 December 2002.

* A/59/150.

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Summary

The Board of Auditors has reviewed the operations of the United Nations capital master plan project. The Board also audited the financial statements of the United Nations, statement IX and schedule 9.1, as they relate to the capital master plan project for the biennium ended 31 December 2003.

The Board's finding is as follows.

Delays in the initiation of the design development and construction documentation phases of the capital master plan may have the following financial impact: an approximate increase of 3.5 per cent in design fees and a rise in administrative and operating expenses for the Office of the United Nations Capital Master Plan of approximately $2.6 million per annum.

A list of the Board's recommendations is contained in paragraph 9 below.

Letter of transmittal

Letter dated 9 July 2004 from the Chairman of the Board of Auditors addressed to the President of the General Assembly

I have the honour to transmit to you the progress report of the Board of Auditors on the capital master plan, in accordance with General Assembly resolution 57/292 of 20 December 2002.

(*Signed*) Shauket A. **Fakie**
Auditor-General of the Republic of South Africa
and Chairman
United Nations Board of Auditors

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I. Introduction

1. The capital master plan fund is reported as part of statement IX, United Nations capital assets and construction-in-progress, of the United Nations financial statements (A/59/5, vol. I). The fund encompasses all expenditures relating to the major refurbishment of the United Nations Headquarters complex in New York. Any unexpended balances of appropriations in the construction-in-progress account are carried forward into succeeding bienniums until the projects are completed.

2. The Board of Auditors has audited the financial statements of the capital master plan as part of its audit of the United Nations for the period from 1 January 2002 to 31 December 2003, in accordance with General Assembly resolution 74 (I) of 7 December 1946. Accordingly, the Board's audit opinion on the financial statements of the United Nations also includes the capital master plan.

3. The Board also reviewed the operations of the capital master plan for the biennium ended 31 December 2003 in response to the request of the General Assembly, in its resolution 57/292 of 20 December 2002, for the Board of Auditors to initiate oversight activities with respect to the development and implementation of the capital master plan and to report annually thereon to the Assembly. This review was conducted in accordance with article VII of the Financial Regulations and Rules of the United Nations and the annex thereto (see ST/SGB/2003/7), the common auditing standards of the Panel of External Auditors of the United Nations, the specialized agencies and the International Atomic Energy Agency and the international standards on auditing.

4. The review was based on the following broad audit objectives as mentioned by the Board in its progress report on the capital master plan (A/58/321, para. 2):

(a) To examine capital master plan financial statements, including an evaluation of project accounting, payment and reporting systems;

(b) To ascertain compliance with United Nations regulations and rules on procurement and contracting;

(c) To determine adherence to the terms of the contract, such as deliverables, time and material provisions;

(d) To review the controls, including internal audit, and processes established to properly manage the project.

5. The review covered the implementation of the "design development" and "construction documentation" phases. The Board recalls that the General Assembly, in its resolution 57/292, noted that the Board of Auditors, in order to avoid a conflict of interest, did not assume responsibility for the validation of initial project costs.

6. The Secretary-General, in his report on the outcome of the capital master plan study (A/57/285 and Corr.1), informed the General Assembly that with the concurrence of the United Nations, the host country's General Accounting Office reviewed the capital master plan project from February to June 2001. The Office concluded, under the heading "Results in brief" of its report entitled "United Nations Headquarters renovation", that the "renovation planning efforts to date,

including the cost estimate, are reasonable" and "have conformed to industry best practices".[1]

7. The present report covers matters that, in the opinion of the Board, should be brought to the attention of the General Assembly. The Board's observations and conclusions were discussed with the Administration, whose views have been appropriately reflected in the report.

8. A summary of the Board's recommendations is contained in paragraph 9 below. The detailed findings and recommendations are reported in paragraphs 20 to 46.

A. Recommendations

9. **The Board recommends that the Administration:**

(a) Comply strictly with United Nations regulations and rules on procurement and contracting (para. 34);

(b) Identify and address all causes of delay in the initiation of the design development and construction documentation phases to ensure their timely completion in an efficient and economical manner (para. 43);

(c) Study and adopt measures to minimize administrative and management costs (para. 45).

B. Background

10. In June 2000, the Secretary-General submitted a report to the General Assembly in which it proposed a major refurbishment of the United Nations Headquarters complex in New York (A/55/117 and Add.1). In that report, the Secretary-General indicated that the current "reactive approach"[2] to maintaining the Headquarters and undertaking the required remedial work as and when needed was inefficient and would become excessively expensive as the buildings aged further. The Secretary-General thus proposed a long-term capital master plan, to be implemented over a period of six years, in a comprehensive, systematic and cost-effective manner. The cost of the capital master plan was estimated at $964 million, consisting of the baseline scope estimate of $902 million and estimated cost for leasing a swing space[3] of $62 million.

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[1] The General Accounting Office updated its report in May 2003 by assessing the revised United Nations renovation plan. The Office recommended that as the capital master plan project progresses additional project management, oversight and monitoring mechanisms would be essential to ensure cost and schedule control and accountability.

[2] One possible approach where the required work is undertaken in a reactive manner over the next 25 years. This means that, as and when building and system failures occur, the required repair work is performed and expenditures incurred.

[3] In order to undertake a major refurbishment programme, large areas must be vacated and the occupants and functions temporarily relocated. The availability of adequate temporary space for meeting, office and support functions, known as "swing space", is therefore indispensable for the implementation of the refurbishment programme.

11. The proposal mentioned three possible sources of funding to meet the costs of the capital master plan: (a) special assessments; (b) the programme budget; and (c) voluntary contributions, in cash or in kind, from public and private sources.

12. The proposal also considered financing options for meeting the costs of the capital master plan: (a) a cash payments option, based on the application of a one-time or multiple-year special assessment; and (b) three deferred payment options. The first deferred payment option is based on the possibility of Member States providing interest-free loans covering the full capital cost requirement. The second option is outside commercial borrowing, at market interest rates, of the full capital cost requirement of $964 million. The third option is premised on the possibility of interest-free loans being available for only a portion of the total capital cost requirement of $964 million, with the balance of the requirement being obtained from outside commercial borrowing.

13. In response to the proposal, the General Assembly, in its resolution 55/238 of 23 December 2000, authorized the Secretary-General, without prejudice to its final decision, to proceed with the preparation of a comprehensive design plan and detailed cost analysis and appropriated $8 million under section 31, Construction, alteration, improvement and major maintenance, of the programme budget for the biennium 2000-2001.

14. In early 2001, a small project team had been established within the Office of the Central Support Services of the Department of Management to carry out the preliminary design phase authorized by the General Assembly. In his report on the outcome of the study, including viable alternatives and measures to prevent cost overruns (A/57/285 and Corr.1), the Secretary-General informed the General Assembly that the comprehensive design plan and detailed cost analysis (referred to as the "preliminary design phase") had been carried out from July 2001 to May 2002.

15. In the same report, the Secretary-General, inter alia, sought authorization from the General Assembly to proceed with the implementation of the capital master plan, starting with design development and construction documentation with estimated costs of $22.5 million for 2003 and $22 million for 2004. He indicated that assuming a design development start date of January 2003 and the required financing is secured, the procurement action for the refurbishment and construction could be initiated as early as July 2004, followed by the initial phases of construction immediately thereafter, in October 2004.

16. The Secretary-General also presented, in annex I of the report, a context diagram of the capital master plan illustrating its various phases and projected time frames: (a) study phase (1998-2000); (b) design phase: preliminary (2001-2002), design development (2003), construction documentation (2004); (c) procurement and construction phase (2005-2010). The overall schedule for the implementation of the plan is, however, dependent on three interconnecting factors: availability of funding; availability of swing space; and progress of technical preparations.

17. The Office of Internal Oversight Services, in its report covering monitoring activities during the period from 1 January to 31 July 2003 (A/58/342), noted that the design development phase was advancing satisfactorily and that there was reasonable assurance indicating that the process thus far has been transparent and fair.

18. At the 45th meeting of the Fifth Committee, on 20 May 2004, the Under-Secretary-General for Management reported that, subject to resolution of various legislative and security approvals, the United Nations Development Corporation[4] hoped to begin construction of its new building on the corner of First Avenue and 42nd Street late in 2005, which was intended to be used as a "swing space". The Secretariat also continued to talk with the host Government and members of Congress regarding an interest-free loan from the United States of America, which still required congressional approval. On 16 March 2004, the United States representative submitted to the Fifth Committee his country's provisional proposal for a $1.2 billion loan at 5.54 per cent interest for a maximum period of 30 years.

19. In respect of funding, the Under-Secretary-General for Management informed the Committee that each of the three components of the capital master plan would be funded differently. The refurbishment of the United Nations complex was the responsibility of the Member States and would be handled by assessments. The Secretariat also hoped to offer Member States the opportunity to fund the refurbishment of specific conference rooms. The construction cost for a new building (UNDC-5) is not a part of the projected budget for the capital master plan, but would be financed separately through the sale of bonds by the United Nations Development Corporation that would not result in any other cost to Member States. The amount that the United Nations would pay to the Development Corporation for the rental of building (UNDC-5) during the implementation of the capital master plan was included in the $1.2 billion plan cost. The major focus for the new Visitors' Centre would be on private-sector financing through various United Nations associations.

II. Financial issues

A. Financial overview

20. The General Assembly, in its resolution 57/292, decided to implement the capital master plan on the basis of the baseline scope under the first approach[5] to phasing and swing space, with a projected construction budget of $1,049 million, a variance of plus or minus 10 per cent, that is, a range estimated at $944.1 million to $1,153.9 million, with a proposed construction start date of October 2004 and a construction duration of five years. The breakdown of the projected construction budget and a comparison with the estimates made in 2000 are set out in table 1 below.

[4] The United Nations Development Corporation is a New York State Public Benefit Corporation that assists the United Nations community with its office space and other real estate needs.

[5] The first approach entails temporary relocation of most of the offices at United Nations Headquarters to a swing space, which would be a new building, to be constructed and owned by the United Nations Development Corporation, on the south-east corner of 42nd Street and First Avenue, thus enabling the refurbishment of the Headquarters complex to be performed in a minimum amount of time.

Table 1
Projected construction budget for the capital master plan
(In millions of United States dollars)

Particulars	*2002*	*2000*
Baseline scope estimate	991	902
Lease cost estimate for swing space	96	62
Decrease in respect of previously approved security measures	(17)	
Decrease in respect of the exclusion of a new large conference room and multi-function hall in the existing complex	(57)	
Addition in respect of the inclusion of the replacement of the curtain wall	36	
Total	**1 049**	**964**

21. The projected construction budget of $1,049 million was further broken down into the components set out in table 2 below.

Table 2
Components of projected construction budget
(In millions of United States dollars)

	Capital master plan	
Components	*Amount*	*Percentage*
Labour and materials	482	46
Planning/design contingency	72	7
General conditions	56	5
Professional fees	98	9
Construction contingency	70	7
Escalation	175	17
Lease cost for swing space	96	9
Total	**1 049**	**100**

22. By the same resolution, the General Assembly authorized the Secretary-General to proceed with the remaining phases of design development and construction documentation and further appropriated $25.5 million for the biennium 2002-2003 for the design and related project management and management of pre-construction services for the baseline scope and scope options. Of this appropriation, $17.9 million (70 per cent) had been allotted for implementation as at 31 December 2003.

23. The General Assembly also authorized the Secretary-General to enter into commitments of up to $26 million for the biennium 2004-2005 to provide for the remaining work related to design and project management.

24. A special account for the capital master plan was also established pursuant to General Assembly resolution A/57/292 and in accordance with the provisions of

regulation 6.6 (now regulation 4.13) of the Financial Regulations and Rules of the United Nations. The separate account was established to manage the appropriation and allotment for the plan.

25. As at 31 December 2003, the budget performance report of the capital master plan showed the following.

Table 3
Budget performance of the capital master plan fund as at 31 December 2003
(In thousands of United States dollars)

Object of expenditure	*Allotment*	*Expenditure*	*Percentage of total expenditure*	*Unencumbered balance*
Staff and other personnel costs	2 299	2 074	48.2	225
Travel	49	44	1.0	5
Contractual services	14 979	1 666	38.7	13 313
Operating expenses	286	289	6.7	(3)
Acquisitions	292	233	5.4	59
Total	**17 905**	**4 306**	**100.0**	**13 599**

26. The actual expenditures of $4.306 million in biennium 2002-2003 increased the total cumulative expenditures for the capital master plan since its inception in December 2000, from $6.881 million in biennium 2000-2001 to $11.187 million as at 31 December 2003.

27. Of the total expenditures, staff costs comprised $2.074 million (48 per cent), operating expenses and acquisitions $0.522 million (12 per cent) and contractual services $1.666 million (39 per cent). The expenditure for staff costs of $2.074 million is 90 per cent of the total allotment for staff costs of $2.299 million, while the commitment for contractual services of $1.666 million is only 11 per cent of the total allotment for contractual services of $14.979 million.

28. The Board expresses its concern on the relatively high staff costs that have been incurred in 2002-2003. The Administration informed the Board that the planned staff costs for 2003 alone, as noted in A/57/7/Add.4 (see annex II — Capital master plan: phase II, design development, and phase III, construction documents), were originally $3.75 million. This figure was reduced as reflected in the allotment, based on the extension of the design phase over a greater number of years. The Administration anticipated that the staff costs for the capital master plan would be close to the planned expenditure and that the total for the completion of design development phase would reach $2.76 million.

B. Write-off of losses of cash, receivables and property

29. In line with financial regulation 6.4, the Administration informed the Board that no cash, receivables or non-expendable property pertaining to the capital master plan project were written off during the biennium ended 31 December 2003.

C. Ex gratia payments

30. The Administration informed the Board, in line with financial regulation 5.11, that no ex gratia payments had been made for the capital master plan fund during the biennium 2002-2003.

III. Management issues

A. Procurement and contracting

31. In its review of contracts pertaining to the design development and construction documentation phases, the Board noted that the Administration was constrained to reimburse the amount of $0.135 million to one contractor for wooden and paper models of the United Nations complex and three dimensional renderings. These were not among the agreed deliverables in its existing contract. They were delivered without prior approval of a specific reimbursable cost amount (in the case of the models) and without prior agreement that the requested product represented a product beyond the base scope requirement (in the case of the renderings).

32. In its memorandum dated 2 July 2003, the Office of Legal Affairs recommended an amicable settlement on the basis that: (a) an arbitral tribunal would likely find that the contractor would be entitled to recover costs to the extent that the contractor could prove and substantiate its claims, since the Organization had received full benefit of the contractor's services for these products, and (b) if the Organization was unable to reach an amicable settlement, it might be found liable not only for the contractor's costs up to $190,000, but also for interest, legal fees and costs for the arbitration.

33. The Board also noted that the Administration granted an exceptional waiver from formal bidding for the landscape design and curtain wall replacement design. In its memorandum dated 10 November 2003, the Administration stated that it decided to grant the waiver "despite a high level of discomfort but for the sake of closure and faced with the time factor". The Board noted that the condition for granting the waiver was not among the exceptions enumerated under paragraph 9.5 of the Procurement Manual and in financial rule 105.16 (a) (ST/SGB/2003/7).

34. **The Administration agreed with the Board's recommendation to comply strictly with the United Nations regulations and rules on procurement and contracting.**

B. Programme management

35. The General Assembly, in its resolution 57/292, requested the Secretary-General to put in place strict control standards for all phases of the capital master plan prior to and during its implementation, defining the precise refurbishment work to be done and the technical results to be achieved so as to ensure, inter alia, (a) that there are no cost overruns associated with the overall project and (b) that the project is completed successfully within the envisaged time frame and budget and within the agreed technical specifications.

36. In his first annual progress report on the implementation of the capital master plan (A/58/599), the Secretary-General stated that the overall schedule for the implementation of the plan is dependent on three interconnecting factors: (a) the availability of funding; (b) the availability of swing space; and (c) the progress of technical preparations. Progress has been made in all areas and all three remain coordinated although behind the initial schedule.

37. The Board noted that out of the six contracts relating to the implementation of the design development and construction documentation phases, no contract had been signed as at 31 December 2003, despite receipt of the proposals on 17 April 2003.

38. As at 31 March 2004, the proposed and revised schedule and actual status of contract signing were as follows:

Table 4
Proposed and revised schedule and actual status of contract signing as at 31 March 2004

Contract	*Proposed schedule*	*Revised schedule*	*Actual status of contract signing*
A. Programme planning services	10 Oct. 2003	7 Jan. 2004	Signed 2 Jan. 2004
B. Infrastructure	25 Nov. 2003	23 Jan. 2004	Draft contract with consultant for review as of 26 March
C. General Assembly and conference buildings	27 Nov. 2003	9 Jan. 2004	Draft contract with Procurement Division
D. Secretariat and South Annex	12 Nov. 2003	15 Jan. 2004	Draft contract with Procurement Division
E. Dag Hammarskjöld Library	10 Dec. 2003	26 Jan. 2004	Draft contract with Procurement Division
F. Security	23 Dec. 2003	5 Feb. 2004	Draft contract with consultant for review as of 26 March

39. The Administration informed the Board that the extended time required at each stage of the procurement and contracting process for the six professional services was a cause of delay in the initiation of the design development and construction documentation phases. The underlying causes were complex as these had to do with the unique nature and speed required for drawing up contracts for implementation of the capital master plan in comparison to the normal pace of engaging consultants at Headquarters. The process of contract finalization required several steps among the consultants, capital master plan staff, the Procurement Division and the Office of Legal Affairs, working together.

40. The Administration also explained that the capital master plan project requires the integration and coordination of three distinctly separate but highly related activities in order to proceed: (a) construction of the UNDC-5 building;

(b) resolution of funding for construction; and (c) development of the capital master plan design documents.

41. Moreover, the Administration was of the view that based on the delay in the schedule for the swing space building (UNDC-5), design activity for the capital master plan should not be completed earlier than required, as this would not be a prudent course of action. Design work should not be completed significantly in advance of bidding. While the detailed schedule should reflect adequate time for review and correction of the design work and for bidding, design work should not be rushed. Design documents must reflect: (a) up-to-the-minute catalogue and model numbers; (b) the latest technology; (c) live information about manufacturers and fabricators; (d) current realities of availability of labour and material types; and (e) actual events in the construction of the swing space.

42. The Administration further informed the Board that the delay in the initiation of the design development and construction documentation phases had no effect on project cost. The only effect would be a potential impact of less than 3.5 per cent of the design fees, which is below the plus or minus 10 per cent variance. In addition, the delay would not affect the implementation of the capital master plan, as the two other interconnecting factors, swing space and funding arrangements, would not be available as scheduled. The critical schedule date (availability of the swing space) has been moved from September 2005, as anticipated in the report of the Secretary-General (A/57/285, issued in August 2002), to the end of January 2008, a delay of 27 months. The effect of the internal delays in the design development and construction documentation phases in comparison to the original schedule is that the United Nations has an additional 15 months to complete the design work.

43. **The Administration agreed with the Board's recommendation that it identify and address all causes of delay in the initiation of the design development and construction documentation phases to ensure their timely completion in an efficient and economical manner.**

44. Administrative and overhead expenses amounting to about $2.6 million (staff costs, $2.1 million; operating expenses and acquisitions, $0.5 million), as discussed in paragraphs 25 to 27 above, would likely be incurred per annum, in addition to the cost overruns on design estimated at 3.5 per cent, as discussed in paragraph 42 above.

45. **The Administration agreed with the Board's recommendation that it study and adopt measures to minimize administrative and management costs during periods of lesser activity, during which time the services of the programme management firm can be suspended.**

C. Cases of fraud and presumptive fraud

46. The Administration informed the Board that there were no cases of fraud and presumptive fraud during the biennium ended 31 December 2003.

IV. Acknowledgement

47. The Board of Auditors wishes to express its appreciation for the cooperation and assistance extended by the Secretary-General, the Under-Secretary-General for Management, the Executive Director of the capital master plan and the members of their staff.

(*Signed*) Shauket A. **Fakie**
Auditor-General of the Republic of South Africa

(*Signed*) Guillermo N. **Carague**
Chairman, Philippine Commission on Audit

(*Signed*) François **Logerot**
First President of the Court of Accounts, France

9 July 2004

Note: The members of the Board of Auditors have signed only the original English version of the report.